

## Applicability of IFRS for SMEs in Kosovo

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### Abstract:

*In many countries of the world, small and medium enterprises (SMEs) have an important position in the local economies. In Kosovo, SMEs constitute approximately 99% of all business entities. Under current law, SMEs are obliged to apply full IFRS, which is a problem because the complexity of these standards. IFRS have been designed for public companies and applying full IFRS for SMEs was a difficult and costly process. SMEs are entities that not have public accountability and publish general purpose financial statements for external users. In July 2009, the International Accounting Standards Board issued IFRS for SMEs, applicable for entities without public interest, to design general financial statements for external users. The IFRS for SMEs is considered as a response for a simpler version of IFRSs. Numerous studies in the field of application of IFRS for SMEs have come to the conclusions that this standard does not leave anything deficient in terms of providing the necessary information to users of financial reporting data from SMEs. The aim of this research is to evaluate the applicability of the IFRS for SMEs in Kosovo, and their readiness to apply this standard. Analysis of the data from empirical research showed that these entities should applying IFRS for SMEs. Based on results of data collected will be given conclusions and recommendations in order to facilitate the work of professionals in the field of accounting and on the other hand to enable a transparent and comparable financial reporting.*

**Key words:** International Financial Reporting Standards (IFRS), IFRS for SMEs, Financial reporting, Small and Medium Sized Entities (SMEs)

## **1. Introduction**

Small and medium-sized enterprises are defined as entities that do not have public accountability and publish general purpose financial statements for external users. Numerous studies in the field of application of IFRS for SMEs have come to the conclusions that this standard does not leave anything deficient in terms of providing the necessary information to users of financial reporting data from SMEs.

Based on current law<sup>1</sup>, in Kosovo since 2011 small and medium-sized entities, that are limited liability companies, are required to apply full IAS and IFRS to the preparation of financial statements. The application of full IFRS, except priorities of the financial reporting, there are some problems in practice due to the complexity of these standards. In terms of Kosovo's economy, the application of these standards becomes complicated and costly. Lack of professional staff for the implementation of these standards increases the problems, especially for small and medium sized entities. The complexity of the full IFRS, frequent changes made in those standards pose numerous problems for SMEs, because they do not have possibility to follow these issues. Engaging of additional staff represents additional costs for these entities.

This study aims to find how much is suitable IFRS for SMEs for small and medium enterprises in Kosovo, and is the standard applicable to the nature and characteristics of SMEs in Kosovo?

This study aims to give answer for following research questions: Is IFRS for SMEs applicable to the Kosovar SMEs? Is IFRS for SMEs suitable to give a true and fair view of SMEs?

We believe that application of the IFRS for SMEs will provide internationally understandable and comparable financial statements in a more simplified and less costly way for SMEs.

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<sup>1</sup> Law nr. 04/L-014, for accounting, financial reporting and auditing

## **2. Literature review**

In the EU, like all around the globe, SMEs have enormous economic significance. In EU Commission vision, small and medium-sized enterprises (SME) are potentially the most dynamic sector of the economy. Their growth is the key for the overall economic well-being. SME represent 99% of all companies in the EU and they provide two-thirds of all private sector jobs. They are the biggest sector of the EU economy, with 23 million enterprises employing around 75 million people. SMEs are responsible for the creation of one in every two new jobs. SME produce considerably more than half the EU's GDP. So, small firms are in fact the real giants of the European economy (Tudor & Mutiu, 2008). SMEs are too significant in the global economy to have been ignored for so long by the international accounting standard setters (Coetzee 2007:32). Since only one set of general purpose IFRSs was developed, SMEs have suffered the cost burden of preparing financial statements based on full IFRSs (Cleminson & Rabin 2002:342)

Collis<sup>2</sup> suggests that larger companies use their financial statements for a wider range of decisions and that they undertake more complex transactions than smaller enterprise, providing aggregated information that requires more sophisticated analysis.

The accounting profession has long struggled with the idea that the financial reporting needs of small, closely held businesses often differ from those required by large, publicly traded companies (Zanzig, & Flesher, 2006).

The IFRS for SMEs is proposed and designed for entities that produce general purpose financial statements to meet the financial reporting needs of small companies and to maintain easy and accurate economic decision making by a broad range of resource providers and other users, such as nonmanager

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<sup>2</sup> Collis J and Jarvis R – How owner-mangers use accounts, centre for Business Performance, ICAEW, 2000.

owners, lenders, vendors, creditors, customers, and employees (Pacter, 2009). The IFRS for SMEs has been simplified and shortened by modifying the accounting standards for the use of SMEs. As a result of all those simplifications, the IFRS for SMEs consists of 230 pages and includes 35 chapters (Walton, 2011)

The IFRS for SMEs is considered to be a significant development which may have strong impact on accounting and auditing practice in the future, but the attitude of national regulators and standard-setters is crucial in establishing the limits of this possible impact (Epstein and Jermakowicz, 2010).

Eierle & Haller (2009) explored the suitability of the IFRS for SMEs for entities of different sizes. The findings of the study indicated that there is no significant relationship between size and assessment of accounting methods. This shows that the IFRS for SMEs is suitable for all types of entities, regardless of their size.

Nerudova & Bohusova (2008) found that the main problem will be the suitability of the IFRS for SMEs for all types of SMEs in the implementation process. According to their study, the first application of the IFRS for SMEs will be expensive and time consuming for the Czech SMEs. On the other hand, the gains are expected to exceed the costs of the IFRS for SMEs implementation.

Neag et al (2009), have found that this global accounting standard may represent a very significant step on the path to global convergence of financial reporting practices by SMEs. It will contribute to enhancing the quality and comparability of SME financial statements around the world and assist SMEs in gaining access to finance.

From the literature review it can be seen that the IFRS for SMEs is adopted for SMEs and it is convenient to provide the necessary and appropriate information for interested parties.

### **3. Methodology**

The first objective of this article is to find out the perception of the practitioners of Kosovo accounting profession about the implementation of the IFRS for SMEs as a reporting framework for the SMEs. For this purpose there have been interviewed the practitioners of accounting profession, accountants and auditors. For this empirical research as population are selected accounting representatives because they understand the client information needs with regard to financial reporting. Another objective of this article was to identify whether accounting representatives believe that the implementation of IFRS for SMEs would reduce the burden of financial reporting of the SMEs.

Previous findings from the review of relevant literature in this field, have served as a basis for the design of the research questionnaire.

**The hypotheses** of this study are based on the findings of previous studies in this area as well as our experience in the field of study. These hypotheses are as follows:

**H1 = IFRS for SMEs is applicable to the Kosovar SMEs**

**H2 = IFRS for SMEs is suitable to give a true and fair view of SMEs**

Based on these hypotheses is designed the research questionnaire, which was sent to the accountants of entities in the period January-February 2014. The questionnaires were sent to 180 businesses, and 52 questionnaires were received and were judged useful for the study. For classification purposes, in the questionnaire is included a section to collect demographic information of the accounting professionals.

#### 4. Analysis, data explanations

To test the hypotheses we have processed and analyzed the results of the data collected.

##### **H1 = IFRS for SMEs is applicable to the Kosovar SMEs**

To test this hypothesis, we have analyzed the responses in our questionnaire regarding applicability of IFRS for SMEs to the Kosovar SMEs. Results are presented in the following table:

**Table no.1 “Is the IFRS for SMEs applicable to the SMEs in Kosovo?”**

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid yes	44	84,6	84,6	84,6
no	6	11,5	11,5	96,2
n/a	2	3,8	3,8	100,0
Total	52	100,0	100,0	

Details regarding the perception of the accounting professionals on the applicability of the IFRS for SMEs show that 84.6 % of respondents think that this standard is applicable in Kosovo. Only 11.5 % of respondents declared that IFRS for SMEs is not applicable to the kosovar SMEs.

As we said above, we can conclude that the hypothesis H1 is confirmed related with that the IFRS for SMEs is applicable for Kosovar SMEs, because 84.6% of respondents claimed the reasonability of hypothesis.

##### **H2 = IFRS for SMEs is suitable to give a true and fair view of SMEs**

To test this hypothesis, we have analyzed the responses in our questionnaire regarding suitability of IFRS for SMEs for giving a true and fair view of SMEs. Results are presented in the following table:

**Table nr. 2 “Is IFRS for SMEs suitable to give a true and fair view of SMEs?”**

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	Frequency	Percent	Valid Percent	Cumulative Percent
Valid no	3	5,8	5,8	5,8
n/a	3	5,8	5,8	11,5
yes	46	88,5	88,5	100,0
Total	52	100,0	100,0	

As was noted in the table above, we can conclude that IFRS for SMEs is suitable to give a true and fair view of SMEs, because 88.5% of respondents answered in favor of suitability of this standard.

***Data analysis related to the suitability of IFRS for SMEs to give a true and fair view of SMEs according to the profession groups of respondents.***

**Table no. 3 Profession\* IFRS for SMEs is suitable to give a true and fair view of SMEs Crosstabulation**

Count

		IFRS for SMEs is suitable to give a true and fair view of SMEs			Total
		no	n/a	yes	
Profession	audit	1	0	6	7
	certif. account.	1	1	22	24
	techn.account.	1	1	7	9
	other	0	1	11	12
Total		3	3	46	52

Data analysis related with suitability of IFRS for SMEs, according to the profession group shows that from the group of auditors, 6 from 7 of them evaluate that IFRS for SMEs is suitable to give a true view of activities of SMEs.

Meanwhile, from profession groups of certified accountants, 22 from 24 of them evaluate as suitable SNRF for SMEs. From the group of accounting technician 7 from 9 of them responded positively in this question. While, the group

the others, 11 from 12 of them think that IFRS for SMEs is suitable to give a true view for activities of SMEs.

**Data analysis for testing the interconnection of variables “IFRS for SMEs is suitable to give a true and fair view of SMEs” and “Profession”:**

Ho: Suitability of IFRS for SMEs and profession are independent

Ha: Suitability of IFRS for SMEs and profession are not independent.

**Table no. 4 Chi-Square Tests - Profession\* IFRS for SMEs is suitable to give a true and fair view of SMEs**

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	3,381 <sup>a</sup>	6	,760
Likelihood Ratio	4,037	6	,672
N of Valid Cases	52		

Variable testing addition from the table above, made through Chi-Square test, shows that variable “IFRS for SMEs is suitable to give a true and fair view for SMEs” is not affected from “profession” of interviewees and from this we can conclude that it hasn’t dependency between two variables, because the value of  $p = 0.760 > 0.05$ , and in this case is confirmed the initial hypothesis on the independence of variables. Thereby we come to the conclusion that IFRS for SMEs is suitable to give a true and fair view of activities of SMEs, something that is evaluated like that, from all groups of respondents despite of their profession, since the interviewees of all groups divided by profession are answered that the standard for SMEs is suitable to offer a financial reporting to satisfy needs of information users from the financial statements.

As we said above we can come to the conclusion that the hypothesis H2 is confirmed related with that the IFRS for SMEs is suitable and sufficient for financial reporting for small



and medium enterprises and in this case 88.5% of the interviewees claimed the justification of hypothesis.

The highlighted reason why small and medium enterprises should apply IFRS for SMEs is because the cost is bigger in comparison with benefits for preparation of financial statements according to full IFRS. Financial statements prepared by full IFRS mainly respond to the needs of the public companies and not to the small and medium non public enterprises.

## **5. Conclusions**

Our findings regarding the applicability of IFRS for SMEs are in accordance with previous studies in this area. Results of this paper show that majority of the respondents, regardless of their profession, are answered that IFRS for SMEs is suitable to give a true and fair view of activities for small and medium enterprises. This is reasonable because IFRS for SMEs is adapted to small and medium enterprises which are entities that not have public accountability and publish general purpose financial statements for external users. This standard considers even the abilities of SMEs to prepare the financial information and the cost of their preparation.

The current accounting law in Kosovo obliges small and medium enterprises to apply the full IAS/IFRS, which is completely unreasonable and illogical. In this way we recommend that the current law on financial reporting in Kosovo to be changed, so that, for small and medium enterprises to enable the implementation of IFRS for SME, because this standard enables the transparent and comprehensive financial reporting.

The implementation of IFRS for SMEs would affect in reducing unnecessary burden to professionals to deal with full IFRS, which are very complex and voluminous. In the other hand, IFRS for SMEs does not leave anything deficient in terms

of providing the necessary information to users of financial reporting data from SMEs.

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